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Letter Ruling 79-34: Lump-Sum Payments to Veterans From a State Pension Plan

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October 4, 1979

You request a ruling with respect to the rate of Massachusetts income taxation of interest accrued on a lump sum payment under the provisions of the Commonwealth of Massachusetts Retirement System dealing with employees who are veterans.

Certain veterans who were employed by the Commonwealth or its subdivisions receive a pension under Massachusetts General Laws Chapter 32, Sections 56-59. In addition, these veterans receive a return of their contributions plus interest in a lump sum payment under Section 25 of Chapter 32. The issue is whether the rate of income taxation is 5% or 10%.

General Laws Chapter 62, Section 2 defines Massachusetts gross income as the federal gross income with certain modifications which are not here relevant. Section 4 of Chapter 62 divides Massachusetts gross income into Part A taxable income, which is taxed at the rate of 10% and Part B taxable income, which is taxed at the rate of 5%. Part A income is composed of dividends, net capital gain, and interest other than interest on Massachusetts savings deposits. Part B income is all other income subject to taxation.

In the instant case the type of income at issue is interest income which is not derived from a Massachusetts savings deposit.

In Daley v. State Tax Commission, a case which involved a lump sum payment from a pension fund, the Supreme Judicial Court found that an earlier version of Chapter 62, which adopted the federal definition of net capital gains and therefore based the rate of income taxation on the year the funds were contributed, violated Article 44 of the Amendments to the Massachusetts Constitution. Article 44 commands a single rate of tax on income from any given class of property.

Addressing itself to the issue of the rate of taxation of income from different classes of property, the Daley Court noted that "the General Court could have drawn a line in the statute between increments on the contributions and the contributions themselves, with different rates applied to the portions of the lump sum payments to taxpayers deriving from the respective sources."

In the case before us, only that portion of the lump sum payment derived from increments on the contributions (interest) is subject to taxation.

Based on the foregoing, it is ruled that the interest portion of a lump sum payment is Part A income and taxable at the rate of 10%.

Very truly yours,

/s/L. Joyce Hampers

L. Joyce Hampers
Commissioner of Revenue

LJH/RSF/jmcd

LR 79-34